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September 23, 2015

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VIA ELECTRONIC FILING

SEP 24 2015

Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th Street SW
Washington, DC 20554

Federal Communications Commission
Office of the Secretary

Re: *Special Access for Price Cap Local Exchange Carriers; WC Docket No. 05-25, RM-10593*

Dear Ms. Dortch:

Pursuant to the Second Protective Order in the above-referenced proceeding, Sprint Corporation ("Sprint") hereby submits a redacted version of the attached Notice of Ex Parte for electronic filing.¹ Highly confidential treatment of the redacted portions of the attached document is required to protect information about Sprint's costs of service and expenditures under particular special access rate structures and plans.² The redacted information is not available from public sources, and "if released to competitors, would allow those competitors to gain a significant advantage in the marketplace."³

In accordance with the Second Protective Order, Sprint will file a hardcopy of the attached document, and deliver two additional hardcopies to Marvin Sacks, Pricing Policy Division, Wireline Competition Bureau, without redaction.

Please contact me if you have any questions or require any additional information.

Sincerely,



Paul Margie
Counsel to Sprint Corporation

¹ *Special Access Rates for Price Cap Local Exchange Carriers*, Second Protective Order, DA 10-2419, 25 FCC Rcd. 17,725 (2010) ("Second Protective Order").

² *See Special Access for Price Cap Local Exchange Carriers*, Letter from Sharon E. Gillett, Chief, Wireline Competition Bureau to Donna Epps, Vice President, Federal Regulatory Affairs, Verizon, DA-12-199, 27 FCC Rcd. 1545 (Feb. 13, 2012) (supplementing the Second Protective Order).

³ *Id.* at 1546.

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Re: *Special Access for Price Cap Local Exchange Carriers; WC Docket No. 05-25, RM-10593*

Dear Ms. Dortch:

Chairman Wheeler recently highlighted the fact that wireless competition hinges on special access reform. On September 9, at CTIA Super Mobility 2015, the Chairman stated: "You [have] to connect all those antennas—and that's a backhaul issue. And that's a special access issue." Sprint Corporation ("Sprint") strongly agrees, and is encouraged that the FCC intends to address the broken special access market in the near term. As Chairman Wheeler stressed: "We need to take a look at just what are the rules governing special access to make sure that somebody who goes out and wants to build new capacity that will increase competition and increase connectivity and increase throughput isn't going to be thwarted."

Chairman Wheeler is correct: special access is a critical input to broadband competition. These dedicated telecommunications services—both TDM and Ethernet—are the backbone for providers who offer wireline and wireless broadband services in competition with incumbents. For wireline broadband services, last-mile special access enables competitors like Sprint to link its Metropolitan Access Networks to businesses located in buildings across the United States. Competitive providers like Sprint have historically relied predominantly on TDM circuits to serve enterprise customers, and today Ethernet has joined TDM as a critical technology for these competitive offerings. As the IP transition builds momentum, Sprint and other providers must have access to both TDM and Ethernet services at reasonable and competitive rates—and the FCC must address both in order to support competition.

In addition, competitive wireless carriers rely on special access for the backhaul links that connect cell sites to the Internet and the switched telephone network. For competitive carriers, backhaul is already an enormous cost center and will be well into the future. Furthermore, as mobile broadband networks transform into a video platform, Ethernet backhaul will continue to grow in importance. The mobile broadband network of the future will require large network "densification" investments to address exploding consumer demand for wireless data services. Densification will require Sprint to deploy tens of thousands of new cell sites. Every one of these sites will require additional backhaul—and Sprint and other competitors will depend on both TDM and Ethernet special access more than ever to be able to compete.

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Addressing unjust special access rates should remain the FCC's main goal—but anticompetitive terms and conditions also constrain the growth of broadband competition. Incumbents dominate the market in which Sprint secures wireless backhaul and building access. They leverage their ownership of backhaul and building access facilities against their competitors, including Sprint, using anticompetitive rates, terms and conditions. In particular, incumbent local exchange carriers (“ILECs”) present their competitors with two choices, each of which undermine competition: competitors can either pay unaffordable month-to-month rates for critical special access services, or agree to so-called “discount” plans that offer reduced, but still grossly inflated, rates in return for the purchaser’s acceptance of competition-killing terms and conditions. The exorbitant rates drive up the cost of a critical input to broadband services, and the terms and conditions limit entry by potential special access competitors.

For example, ILECs use terms that impose loyalty commitments based on the customer’s prior purchases from the ILEC to hoard demand from competing providers. If the purchaser fails to meet its loyalty commitment, it faces punitive “shortfall” charges, which can exceed, by many multiples, even the ILEC’s prohibitive undiscounted rates. These loyalty commitments ensure that purchasers do not switch to alternative special access providers in the limited geographic areas where alternatives are available or could potentially arise. Many ILECs also charge “overage” penalties if a purchaser exceeds its commitment levels—that is, unless the purchaser agrees to raise its commitment levels. These overage penalties ensure that purchasers commit incremental increases in demand to the ILEC, which prevents growing companies from spurring entry by an alternative special access provider. Moreover, ILECs have long imposed excessive early termination fees designed to penalize purchasers for seeking and choosing alternative access vendors in the limited instances where an alternative vendor is available.

There are only two ways to escape these oppressive terms and conditions: (1) terminate service with the incumbent in favor of an alternative provider and pay enormous penalties because of ILEC contractual terms, or (2) allow the “discount” plans to expire and pay the ILEC’s exorbitant month-to-month rates. As discussed below, Sprint has taken both of these paths in an effort to reduce dependence on ILEC special access services, and it has paid—and will continue to pay—an enormous price for doing so, reducing its ability to compete.

These claims are not theoretical. They come from the trenches. As discussed below, ILEC abuse of their special access dominance through excessive rates and anticompetitive terms undermines Sprint’s ability to compete by (1) imposing huge and asymmetric costs on competitors’ access to a key competitive input through penalty clauses and uneconomic rates; (2) preventing competitors in the enterprise broadband market from offering competitive rates by inflating their underlying costs to levels that lead to price squeeze behavior; and (3) adopting unreasonable penalties and facially anticompetitive terms in the Ethernet contracts that competitors need to advance the IP transition.

The combination of these real-world harms means that the future of both retail wireless and enterprise wireline broadband competition depends on the FCC’s special access proceeding.

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The Commission therefore should take immediate action to eliminate the stranglehold that ILECs have placed on the special access market. Without Commission action to eliminate anticompetitive terms and conditions for TDM and Ethernet special access, and action to reduce rates to just and reasonable levels, it will be extraordinarily difficult for the special access market ever to become fully competitive in areas where additional entry is economically feasible. In turn, broadband competition will suffer.

I. ILEC Use of Unjust and Unreasonable Terms and Conditions.

The interaction of anticompetitive terms and conditions and unreasonable rates in special access contracts substantially undermines competition not only in the special access market, but also in wireline enterprise and wireless broadband markets. While Sprint has discussed rates in previous FCC filings, in this filing we concentrate on terms and conditions.

For many years, ILECs have utilized an array of anticompetitive terms and conditions to entrench their dominance in the provision of the special access circuits. The ILEC strategy is simple: ILECs use their dominance in the special access market to charge extraordinarily high month-to-month, or “rack” rates that purchasers generally cannot afford to pay. Competitors must undermine their own ability to compete by accepting these rates, or signing onto deceptively named “discount plans” offered by the incumbent that include non-negotiable and anticompetitive terms and conditions that serve to strangle special access competition and therefore ensure that ILEC dominance continues.¹

At the heart of anticompetitive ILEC terms and conditions are loyalty commitments, which require purchasers to maintain their special access purchases at consistent levels.² The commitment levels are typically set, not based on specific volumes that trigger economies of scale, but rather on the customer’s historic special access purchases from the ILEC, which simply ensures that customers remain loyal to the ILEC. If a purchaser misses its loyalty commitment, which can be as high as 100% of the purchaser’s prior purchases, the ILEC will charge a draconian shortfall penalty, which can exceed—by many times—the cost of simply leaving the circuits in service.³ Some plans may allow purchasers to reduce their commitments, but only through payment of an equally draconian “buy-down” fee, which likewise can greatly

¹ For a detailed description of the harmful terms and conditions that Sprint faces in each applicable tariff, see Sprint Corporation’s responses to Questions II.E.9 and II.F.8 of the Commission’s recent mandatory special access data collection.

² See, e.g., Comments of Sprint Nextel Corporation at 23-27, WC Docket No. 05-25, RM-10593 (filed Feb. 11, 2013).

³ See *id.* at 30-32.

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exceed the cost of simply leaving the circuits in service.⁴ Thus, once a commitment is established, special access purchasers like Sprint cannot reduce their purchase levels in favor of a competitor's service without suffering significant penalties. This, in turn, serves as a disincentive to market entry by providers who may otherwise seek to enter the market to provide a competitive alternative.

II. Anticompetitive Terms and Conditions Have Significant Impact on Wireline and Wireless Broadband Competition.

The combination of excessive special access prices and anticompetitive terms produces a real-world impact on broadband competition. These circuits are critical inputs to Sprint's wireline enterprise and wireless products. As discussed below, the broken special access regulatory system allows ILECs to undermine competition by Sprint and others in both of these markets.

A. ILECs Leverage Their Special Access Dominance to Raise Their Enterprise-Broadband Rivals' Costs in the IP Transition.

As a consequence of the ILECs' hundred-year dominance over last-mile networks, Sprint must rely on its chief broadband competitors to acquire a critical input to its services: last-mile special access services. For many years, Sprint has therefore purchased thousands of both DSN and Ethernet lines from Verizon, AT&T, and other ILECs. In an effort to remain competitive and transition to an IP network, Sprint has invested in converting many of its TDM lines to Ethernet. The result is that both DSN and Ethernet lines are now core competitive inputs for Sprint and other competitors.

ILEC rates, terms, and conditions have imposed an enormous cost on Sprint as it works to make this transition in the broadband services it provides to enterprise customers. As the Commission understands, no provider can transition to IP across its entire footprint overnight. But ILEC loyalty plans put purchasers in an "all or nothing" situation. If a buyer does not continue to purchase, for example, 90 percent of its previous number of TDM lines from the ILEC, it faces huge penalties. Sprint therefore has been forced to begin removing *all* of its TDM circuits from each separate ILEC loyalty plan as it makes its transition, in order to avoid the crushing penalties that would result from converting to Ethernet only the *fraction* of access circuits needed at each stage of the transition.

Not all of Sprint's enterprise customers are willing to or can convert to Ethernet instantly. Nor is fiber Ethernet access ubiquitously available at all business locations. And the number of buildings with more than one Ethernet access vendor is even smaller. The consequence is that

⁴ See *id.* at 30, 32.

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Sprint must re-purchase all special access circuits that remain TDM at the patently unreasonable rates available without loyalty provisions to avoid ILEC loyalty commitments that would lock Sprint into TDM-based services far into the future. Consider the magnitude of the cost of moving from already exorbitant "loyalty" rates to rack rates for competitors: Verizon's rates are 40 percent higher and AT&T's rates are up to 65 percent higher. Based on Sprint's current TDM access circuit demand with these carriers, the annual increase in cost is estimated to exceed ***
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CONFIDENTIAL *** So far, this has already imposed a cost on Sprint's IP conversion of ***
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*** since December 2014.

ILECs' ability to raise Sprint's costs in this manner has an important additional consequence. These rapidly increasing critical input costs undermine Sprint's ability to compete in ongoing bids in the enterprise broadband market—and can result in Sprint losing existing enterprise customers due to ILEC price squeeze behavior. Recently, for example, Sprint lost a longtime enterprise broadband customer because an ILEC undercut Sprint's pricing by nearly \$1 million per year because the ILEC's *retail rates* were less than the inflated wholesale access *costs* that Sprint must pay for last-mile special access circuits, including circuits from the same ILEC.⁵ As a result of its control over special access rates, the ILEC therefore was able to eliminate Sprint as a competitor for enterprise broadband service to a business that had been pleased with Sprint's services for nearly ten years. Moreover, the loss of this customer's wireline business severely jeopardizes Sprint's ability to win the customer's wireless business. In short, the ILEC's control over last-mile access allows it to undermine competition for enterprise landline, enterprise wireless, and integrated wireline and wireless communications services.

The same dynamic undermined Sprint's attempts to offer the benefit of its more efficient network services to U.S. taxpayers. Major telecommunications providers, including Sprint, have bid on "Networx" contracts to supply network services to the federal government. In the Networx bids Sprint examined, two components determined the contract price: an access component, reflecting the cost of special access facilities required to reach the government site, and a port charge, reflecting the costs associated with using the bidder's network.⁶ The bids exposed that ILECs were *pricing retail access services well below the wholesale access price* they made available to Sprint. As a result, even though Sprint's port charge was lower than the

⁵ Last-mile special access circuit prices typically account for well over 60% of the total retail rate. As a result, ILECs, due to owner's economics and insider knowledge of the majority of their competitors' costs, are able to manipulate their retail price offer in order to undercut competitors and win the business.

⁶ See Comments of Sprint Nextel Corporation, WC Docket No. 10-188 (filed Oct. 15, 2010).

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winning ILEC's port charge, Sprint could not overcome its artificially inflated costs of access. Sprint lost the bid, and taxpayers lost the benefit of receiving competitive rates for both access and network operations.⁷

B. ILEC Special Access Terms and Conditions and Unreasonable Rates Have Raised Their Wireless Broadband Competitors' Costs.

Special access terms and conditions also create a severe cost disadvantage for Sprint's wireless business. Because of these terms and conditions, the cost of Sprint's transition to Ethernet backhaul has been staggering. Through its Network Vision project, Sprint optimized its wireless network by upgrading the backhaul connections to approximately 38,000 macrocell sites. Because of the unique magnitude of this project, Sprint was able to issue an RFP that solicited bids from multiple providers to provide backhaul services to many of its sites.⁸ This enormous and unique process was an effort to put all of Sprint's circuits together to attract competitive response. Because Sprint is specially positioned as likely the largest non-ILEC backhaul purchaser in the country, it was able to contract with competitive providers in some markets. But ILEC terms and conditions imposed a huge cost on Sprint for attempting to purchase from competitors. From 2013 to 2014, Sprint paid more than *** **BEGIN HIGHLY CONFIDENTIAL** *** [REDACTED] *** **END HIGHLY CONFIDENTIAL** *** in penalties to ILECs in order to escape anticompetitive terms, just for the right to purchase from competitors in some markets.

These costs represent a heavy blow for even a company as large as Sprint and could not be borne by the vast majority of broadband purchasers. Sprint was willing to incur these penalties, which depleted funds needed to compete with Verizon and AT&T, only because it was committed to a massive project that would optimize its entire wireless network. Under normal circumstances, ILEC shortfall penalties prevent choosing competitors, and the Network Vision figures show why. Indeed, Sprint in the past has purchased a number of costly but pointless "circuits to nowhere" just to avoid such onerous penalties.

⁷ See *id.*

⁸ As discussed previously in this proceeding, the Network Vision project does not reflect the reality of the special access market. Sprint was able to contract with competitive providers in limited markets only because of the scope and scale of the project. In day-to-day reality, purchasers—including Sprint—are not able to purchase anything approaching the volume of circuits Sprint put out for bid in Network Vision, and thus are unable to attract sufficient interest from competitive providers to spur competitive entry. See Letter from Paul Margie, Counsel to Sprint Nextel Corporation, to Marlene H. Dortch, Secretary, FCC, at 5-6, WC Docket No. 05-25 (filed Sept. 26, 2012).

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C. ILECs Are Imposing Anticompetitive Terms and Conditions on New Ethernet Contracts.

Ethernet special access contracts have already begun to include anticompetitive terms and conditions. Examining some of these terms demonstrate why the Commission must address terms and conditions across both TDM and Ethernet services.

First, many ILEC Ethernet contracts impose enormous early termination penalties that bear no relationship to supplier costs and have no plausible economic rationale other than to deter competitive choice. If Sprint tried to switch the Ethernet circuits it currently leases for backhaul from ILECs to competitive providers, it would face more than *** **BEGIN HIGHLY CONFIDENTIAL** *** [REDACTED] *** **END HIGHLY CONFIDENTIAL** *** in potential penalties. The likelihood of stable, competitive markets for Ethernet will only decrease as special access demand flows to agreements with oppressive terms and conditions, given the size of the penalties at issue.

Second, ILECs work to exploit their historical dominance of DSN services to capture the rising demand for Ethernet services. As companies like Sprint upgrade their special access services from TDM-based circuits to IP-based services like Ethernet, they face the option of either (1) purchasing Ethernet services solely from ILECs, or (2) purchasing Ethernet from an alternative provider and incurring significant early termination and shortfall penalties from the ILECs. Indeed, Sprint historically purchased nearly all of its TDM-based backhaul services from ILECs pursuant to discount plans that include the loyalty commitments discussed above, as well as term commitments that can be as high as seven years. As seen with its Network Vision project, conversion from TDM to Ethernet reduced Sprint's TDM purchases, which triggered shortfall penalties, in addition to any early termination liabilities caused by terminating TDM circuits before the applicable term expired. Sprint has paid a heavy price and, like many other providers, is still tightly tied to ILEC special access.

Outside of the unique Network Vision context the situation is even worse. The typical special access purchaser is more likely to rely on ILEC "technology migration" plans, through which the ILEC waives shortfall and early termination liabilities, *so long as the purchaser buys the upgraded service (such as Ethernet) from the ILEC*. In this way, the ILEC ensures that it captures demand for upgraded technologies. In order to remain competitive in the wireless business, most purchasers will be forced to purchase Ethernet from the ILEC instead of paying the astronomical penalties associated with buying Ethernet from an alternative provider.

Third, Ethernet contracts are now beginning to contain new restrictive terms and conditions. As discussed above, punishing, non cost-based early termination charges are common. But there are other examples of facially anticompetitive terms that also seek to prohibit Sprint from switching services to a competitor. For example, under certain contracts, if Sprint decided to forgo a given Ethernet circuit, then it must agree to either self-provision, or continue to use existing TDM-based services rather than switch to an alternative Ethernet

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provider. In another example, as a condition for collocating on an affiliate tower, Sprint would be required to utilize the ILEC's services rather than a competitive backhaul provider.

Through years of enforcing oppressive terms and conditions, ILECs have leveraged their last-mile facilities dominance to control TDM-based special access services to the detriment of providers who compete with ILEC wireline and wireless broadband service offerings. As the availability and use of IP-based services such as Ethernet continue to expand, the Commission should take this opportunity to prevent history from repeating itself. ILEC terms and conditions are still subject to Sections 201 and 202 of the Communications Act regardless of whether the terms appear in a tariff for TDM-based special access services or in a contract for Ethernet special access services.⁹ Accordingly, ILECs are prohibited from imposing unjust and unreasonable terms and conditions on both TDM and Ethernet purchases. The Commission should make clear that the ILEC practice of cementing last-mile facilities dominance through anticompetitive terms and conditions, including but not limited to economically irrational early termination fees, loyalty commitments, shortfall penalties, buy-down fees, and overage penalties, is unjust and unreasonable in violation of Sections 201 and 202 of the Communications Act¹⁰—regardless of the service to which the terms and conditions apply, and regardless of the vehicle through which they are imposed. The ILECs should not be allowed to use their historical market dominance in TDM services, achieved when they were not subject to the market opening measures in the Telecommunications Act of 1996, as a tool to achieve dominance in the new and evolving market for Ethernet backhaul and enterprise building access. In order to encourage the development of wholesale last-mile access competition in areas where competitive entry is economically feasible, and to eliminate the diversion of scarce financial resources away from competitive infrastructure investment to the coffers of entrenched incumbents, the Commission must prohibit unjust and unreasonable terms and conditions.

* * *

For the reasons detailed above, Sprint urges the Commission to move rapidly to address anticompetitive special access terms and conditions. But eliminating anticompetitive terms and conditions is one of two steps the Commission must take to repair the broken special access market. In many areas, competition will never arise, even in the absence of anticompetitive terms and conditions. And in areas where competition does develop, it will not happen overnight, and it may not be sufficient to establish just and reasonable special access rates.

⁹ See, e.g., *Petition of AT&T Inc. for Forbearance Under 47 U.S.C. § 160(c) from Title II and Computer Inquiry Rules with Respect to Its Broadband Services*, Memorandum Opinion and Order, FCC 07-180, 22 FCC Rcd. 18,705, at ¶ 35 (2007) (“AT&T will continue to be subject to sections 201 and 202 of the Act in its provision of its specified broadband services”).

¹⁰ See 47 U.S.C. §§ 201(b) (requiring that all ILEC “charges [and] practices ... shall be just and reasonable”); 202(a) (prohibiting all “unjust or unreasonable discrimination”).

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Indeed, Sprint was generally unable to obtain competitive rates as part of its Network Vision project, even in areas where an alternative provider submitted the winning bid.

There are very few geographic areas where simply eliminating anticompetitive terms and conditions will help because ILECs will continue to maintain competition-killing rates. Accordingly, the Commission should also act expeditiously to analyze the data submitted in response to the special access data collection, rationalize prices in areas where ILECs have received Phase II pricing flexibility, and establish price caps that reflect just and reasonable rates for special access services.

Sincerely,

A handwritten signature in cursive script, appearing to read "A.P. Margie".

Paul Margie
Walter Anderson
V. Shiva Goel
Counsel to Sprint Corporation